

May 21, 2004

To: Governor Kathleen Sebelius and Legislative Budget Committee
From: Chris W. Courtwright, Principal Economist
Re: Legislative Adjustments to Consensus Estimates for FY 2004 and FY 2005

Pursuant to KSA 75-6701, the Legislative Research Department and Division of the Budget have adjusted the most recent estimates of State General Fund (SGF) receipts for FY 2004 and FY 2005. These adjustments reflect the fiscal impact of legislation involving receipts to the SGF enacted during the 2004 Legislative Session subsequent to the Consensus Revenue Estimate made on April 20, 2004. The attached tables show changes by source and incorporate those changes into the overall estimate for the fiscal year. FY 2004 receipts were increased by \$0.150 million relative to the April estimate, attributable entirely to a change in transfers. FY 2005 receipts were decreased by \$0.679 million below the April estimate. The net adjustment for both fiscal years combined is a reduction of \$0.529 million.

The estimated impact of a new federal law has **not** been included in these revisions, which by law are to include only those changes attributable to Kansas legislation. The Department of Revenue has indicated that the exemption from state taxation for certain telecommunications services used to provide Internet access, one provision of the new federal law, will be expected to **reduce SGF sales tax receipts by an additional \$10 million in FY 2005** relative to the adjusted estimate contained in this document.

An additional section also has been added to this report discussing the implications for SGF receipts for FY 2006 and subsequent years relative to Kansas legislation enacted prior to April 20 (in some cases, several years before) as well as during the veto session.

The Consensus Group will meet again prior to December 4 to consider revisions to the newly adjusted FY 2005 estimate and to make an initial estimate for FY 2006.

FY 2004

Net SGF transfers were increased by \$0.150 million pursuant to an increase in transfers from the Insurance Department Service Regulation Fund enacted in the omnibus bill (S Sub HB 2471).

FY 2005

The following FY 2005 adjustments were made:

- ! House Sub. SB 147 provided for a number of new sales tax exemptions, effective January 1, 2005, which will collectively reduce receipts by \$5.369 million for the balance of the fiscal year. One of the exemptions for certain aircraft repair and replacement parts, which is expected to reduce receipts by \$0.7 million, is expected to reduce sales and compensating use tax receipts by

\$0.35 million each. Filing deceleration provisions also will reduce receipts by an additional \$1.8 million, with \$1.44 million attributable to the sales tax and \$0.36 million attributable to the use tax. A change in the tax treatment of certain isolated and occasional sales of motor vehicles is estimated to increase receipts by \$2.0 million. The net adjustment to sales and use tax receipts is therefore a reduction of \$5.169 million. Income tax provisions relating to estimated tax penalties and Homestead property tax refunds are expected to reduce receipts by \$0.196 million. Finally, changes in franchise taxes are expected to increase total franchise tax and fee receipts by \$5.3 million.

- ! Senate Sub. HB 2471, the omnibus bill, also decreased the estimate for net transfers by \$0.170 million. Transfers from the Insurance Department Service Regulation Fund were increased by \$0.080 million; but additional transfers for the Emergency Medical Services Education Incentive Project and the Military Emergency Relief Fund of \$0.200 million and \$0.050 million, respectively, were enacted in the same bill.
- ! One provision of S Sub HB 2375, which requires the suspension or revocation of vehicle dealers' licenses when such dealers are delinquent in sales or withholding taxes for three consecutive months, is expected to increase receipts by \$0.5 million (\$0.4 million in sales tax receipts and \$0.1 million in individual income taxes).
- ! SB 552 reduced the amount of agency earnings for the SGF by \$0.944 million pursuant to a provision that increased the amount of certain fines and forfeitures earmarked instead for the Crime Victims' Compensation Fund.

One other bill may affect FY 2005 receipts, but its impact was not quantifiable.

- ! HB 2682, which provides a number of requirements for individuals and companies selling cigarettes over the Internet, telephone, or by any other type of mail-order transaction, could provide for slight but unspecified increases in cigarette, sales, and use tax revenues.

FY 2006 and Thereafter

Several other bills are expected to have an impact on SGF receipts, but the provisions are not effective until after the end of the current consensus estimates (FY 2005).

- ! Learning Quest Program Expansion. HB 2795 includes a significant expansion of the state income tax deduction associated with the Learning Quest (Internal Revenue Code section 529) education savings program. Starting in tax year 2005, the maximum income tax deduction for qualifying contributions is increased from \$2,000 to \$3,000 for each beneficiary of a single individual income taxpayer; and from \$4,000 to \$6,000 for each beneficiary of joint filers. Receipts in FY 2006 are expected to be reduced by \$2.0 million as a result of this provision.
- ! Deduction for Certain Premiums. HB 2545 allows in the determination of Kansas adjusted gross income for tax year 2005 a deduction from federal

adjusted gross income of up to \$500 for certain long term care insurance premiums. The amount of the maximum deduction then increases to \$1,000 over the next five tax years. The estimated reduction in SGF receipts is \$1.4 million in FY 2006; \$1.7 million in FY 2007; \$1.9 million in FY 2008; \$2.2 million in FY 2009; \$2.5 million in FY 2010; and \$2.8 million in FY 2011 and thereafter.

- ! Less Sales/Use Tax to SGF. SB 384 reduces the SGF's share of the 5.3 percent sales and use taxes from the current 95.28 percent to 92.83 percent in FY 2007; and 87.74 percent in FY 2008 and thereafter. Even after accounting for the fact that the legislation also maintained the tax rate at 5.3 percent on and after July 1, 2006 (when it had been scheduled to be reduced to 5.0 percent), SGF receipts will be reduced by about \$117.4 million for the FY 2007-FY 2011 period as a result of the changes.
- ! Refundable income tax credits. Legislation enacted in 2002 increased the refundable tax credits available to help offset certain property taxes on commercial and industrial machinery and equipment from 15 percent to 20 percent in tax year 2005; and to 25 percent in tax year 2007 and thereafter. The 2002 legislation also for the first time extended the availability of the credits to certain railroad property. The estimated fiscal impact relative to the increase in the amount of credits claimed is \$12.673 million in FY 2006; \$13.800 million in FY 2007; and \$18.796 million in FY 2008 (when the 25 percent level is fully phased in).
- ! STAR Bond Redevelopment Districts. As the Consensus Group noted in April, another issue affecting the growth of SGF sales tax receipts is the diversion of revenues to the city bond finance fund relative to the redevelopment district in Kansas City, Kansas. City bond finance fund receipts are likely to exceed \$15 million for FY 2004, a significant increase from \$4.1 million in FY 2003 and \$1.5 million in FY 2002. Legislation enacted in 2003 also made it more likely that additional redevelopment districts with the potential to divert SGF receipts would be established.
- ! Bioscience Industry Legislation. A number of provisions in the Kansas Economic Growth Act, especially those relating to the future diversion from the SGF of revenue streams attributable to the biosciences industry, also have the potential to reduce SGF receipts over time.
- ! Estate Taxes. Pursuant to legislation enacted in 2003, estate tax receipts will be reduced by \$8.5 million in FY 2008 and by \$11.2 million in FY 2009 as a result of Kansas' conforming to the federal estate tax exemption threshold.
- ! Impact of 2004 Legislation. Franchise taxes and fees are expected to increase by an additional \$4.0 million above the FY 2005 amount, but receipts from sales and use taxes are expected to decrease by a similar amount (as a result of the annualized impacts of the new exemptions).

TABLE 1
State General Fund Receipts
(In Thousands)

Adjusted for Legislation Enacted After April 20, 2004

	FY 2003			FY 2004 (Revised)			FY 2005 (Revised)	
	Amount	Percent Increase		Amount	Percent Increase		Amount	Percent Increase
Property Tax:								
Motor Carrier	\$15,729	(12.9)	%	\$19,000	20.8	%	\$19,500	2.6 %
General Property	0	0.0		13,600	---		400	(97.1)
Motor Vehicle	0	0.0		1,500	---		1,000	(33.3)
Total	\$15,729	(12.9)	%	\$34,100	116.8	%	\$20,900	(38.7) %
Income Taxes:								
Individual	\$1,750,054	(4.3)	%	\$1,830,000	4.6	%	\$1,899,904	3.8 %
Corporation	105,222	12.0		125,000	18.8		130,000	4.0
Financial Inst.	31,120	11.5		34,000	9.3		34,500	1.5
Total	\$1,886,396	(3.3)	%	\$1,989,000	5.4	%	\$2,064,404	3.8 %
Estate/Succession	\$46,952	(2.4)	%	\$48,000	2.2	%	\$49,000	2.1 %
Excise Taxes:								
Retail Sales	\$1,567,722	6.6	%	\$1,620,000	3.3	%	\$1,670,941	3.1 %
Compensating Use	225,923	(3.3)		212,000	(6.2)		224,290	5.8
Cigarette	129,250	169.0		120,000	(7.2)		118,000	(1.7)
Tobacco Prod.	4,510	4.8		4,800	6.4		4,900	2.1
Cereal Malt Bev.	2,273	(4.5)		2,200	(3.2)		2,200	0.0
Liquor Gallonage	14,802	1.2		15,600	5.4		16,000	2.6
Liquor Enforce.	38,833	3.8		41,000	5.6		42,000	2.4
Liquor Dr. Places	6,847	3.5		7,400	8.1		7,700	4.1
Corp. Franchise	31,090	67.9		36,000	15.8		42,300	17.5
Severance	72,775	30.7		80,600	10.8		77,600	(3.7)
Gas	56,261	34.6		62,200	10.6		58,900	(5.3)
Oil	16,515	18.9		18,400	11.4		18,700	1.6
Total	\$2,094,025	10.7	%	\$2,139,600	2.2	%	\$2,205,931	3.1 %
Other Taxes:								
Insurance Prem.	\$94,455	11.2	%	\$100,000	5.9	%	\$100,000	0.0 %
Miscellaneous	4,427	82.9		4,500	1.6		4,500	0.0
Total	\$98,882	13.2	%	\$104,500	5.7	%	\$104,500	0.0 %
Total Taxes	\$4,141,984	3.6	%	\$4,315,200	4.2	%	\$4,444,735	3.0 %
Other Revenues:								
Interest	\$19,075	(50.7)	%	\$14,300	(25.0)	%	\$21,500	50.4 %
Net Transfers	(13,036)	---		20,050	(253.8)		11,530	(42.5)
Ag. Earn. & Misc.	97,556	89.5		100,900	3.4		63,956	(36.6)
Total Other Revenue	\$103,595	(7.5)	%	\$135,250	30.6	%	\$96,986	(28.3) %
Total Receipts	<u>\$4,245,579</u>	3.3	%	<u>\$4,450,450</u>	4.8	%	<u>\$4,541,721</u>	2.1 %

TABLE 2
State General Fund Receipts – Comparison of Estimates for FY 2004

	CRE Estimate 4/20/04	Adjusted Estimate 5/21/04	Difference
Property Tax:			
Motor Carrier	\$19,000	\$19,000	\$0
General Property	13,600	13,600	0
Motor Vehicle	1,500	1,500	0
Total	\$34,100	\$34,100	\$0
Income Taxes:			
Individual	\$1,830,000	\$1,830,000	\$0
Corporation	125,000	125,000	0
Financial Inst.	34,000	34,000	0
Total	\$1,989,000	\$1,989,000	\$0
Estate/Succession	\$48,000	\$48,000	\$0
Excise Taxes:			
Retail Sales	\$1,620,000	\$1,620,000	\$0
Compensating Use	212,000	212,000	0
Cigarette	120,000	120,000	0
Tobacco Prod.	4,800	4,800	0
Cereal Malt Bev.	2,200	2,200	0
Liquor Gallonage	15,600	15,600	0
Liquor Enforce.	41,000	41,000	0
Liquor Dr. Places	7,400	7,400	0
Corp. Franchise	36,000	36,000	0
Severance	80,600	80,600	0
Gas	62,200	62,200	0
Oil	18,400	18,400	0
Total	\$2,139,600	\$2,139,600	\$0
Other Taxes:			
Insurance Prem.	\$100,000	\$100,000	\$0
Miscellaneous	4,500	4,500	0
Total	\$104,500	\$104,500	\$0
Total Taxes	\$4,315,200	\$4,315,200	\$0
Other Revenues:			
Interest	\$14,300	\$14,300	\$0
Net Transfers	19,900	20,050	150
Ag. Earn. & Misc.	100,900	100,900	0
Total Other Revenue	\$135,100	\$135,250	\$150
Total Receipts	<u>\$4,450,300</u>	<u>\$4,450,450</u>	<u>\$150</u>

TABLE 3
State General Fund Receipts – Comparison of Estimates for FY 2005

	CRE Estimate 4/20/04	Adjusted Estimate 5/21/04	Difference
Property Tax:			
Motor Carrier	\$19,500	\$19,500	\$0
General Property	400	400	0
Motor Vehicle	1,000	1,000	0
Total	\$20,900	\$20,900	\$0
Income Taxes:			
Individual	\$1,900,000	\$1,899,904	(\$96)
Corporation	130,000	130,000	0
Financial Inst.	34,500	34,500	0
Total	\$2,064,500	\$2,064,404	(\$96)
Estate/Succession	\$49,000	\$49,000	\$0
Excise Taxes:			
Retail Sales	\$1,675,000	\$1,670,941	(\$4,059)
Compensating Use	225,000	224,290	(710)
Cigarette	118,000	118,000	0
Tobacco Prod.	4,900	4,900	0
Cereal Malt Bev.	2,200	2,200	0
Liquor Gallonage	16,000	16,000	0
Liquor Enforce.	42,000	42,000	0
Liquor Dr. Places	7,700	7,700	0
Corp. Franchise	37,000	42,300	5,300
Severance	77,600	77,600	0
Gas	58,900	58,900	0
Oil	18,700	18,700	0
Total	\$2,205,400	\$2,205,931	\$531
Other Taxes:			
Insurance Prem.	\$100,000	\$100,000	\$0
Miscellaneous	4,500	4,500	0
Total	\$104,500	\$104,500	\$0
Total Taxes	\$4,444,300	\$4,444,735	\$435
Other Revenues:			
Interest	\$21,500	\$21,500	\$0
Net Transfers	11,700	11,530	(170)
Ag. Earn. & Misc.	64,900	63,956	(944)
Total Other Revenue	\$98,100	\$96,986	(\$1,114)

Total Receipts

\$4,542,400

\$4,541,721

(\$679)

TABLE 4
Legislative Adjustments by Bill by Source to FY 2005 Consensus Estimates
(\$ in millions)

	Sales	Use	Individual Income	Franchise	Net Transfers	Agency Earnings	SGF Total
H Sub SB 147	\$(4.459)	\$(0.710)	\$(0.196)	\$5.300	---	---	\$(0.065)
S Sub HB 2471	---	---	---	---	\$(0.170)	---	\$(0.170)
S Sub HB 2375	\$0.400	---	\$0.100	---	---	---	\$0.500
SB 552	---	---	---	---	---	\$(0.944)	\$(0.944)
Total	\$(4.059)	\$(0.710)	\$(0.096)	\$5.300	\$(0.170)	\$(0.944)	\$(0.679)